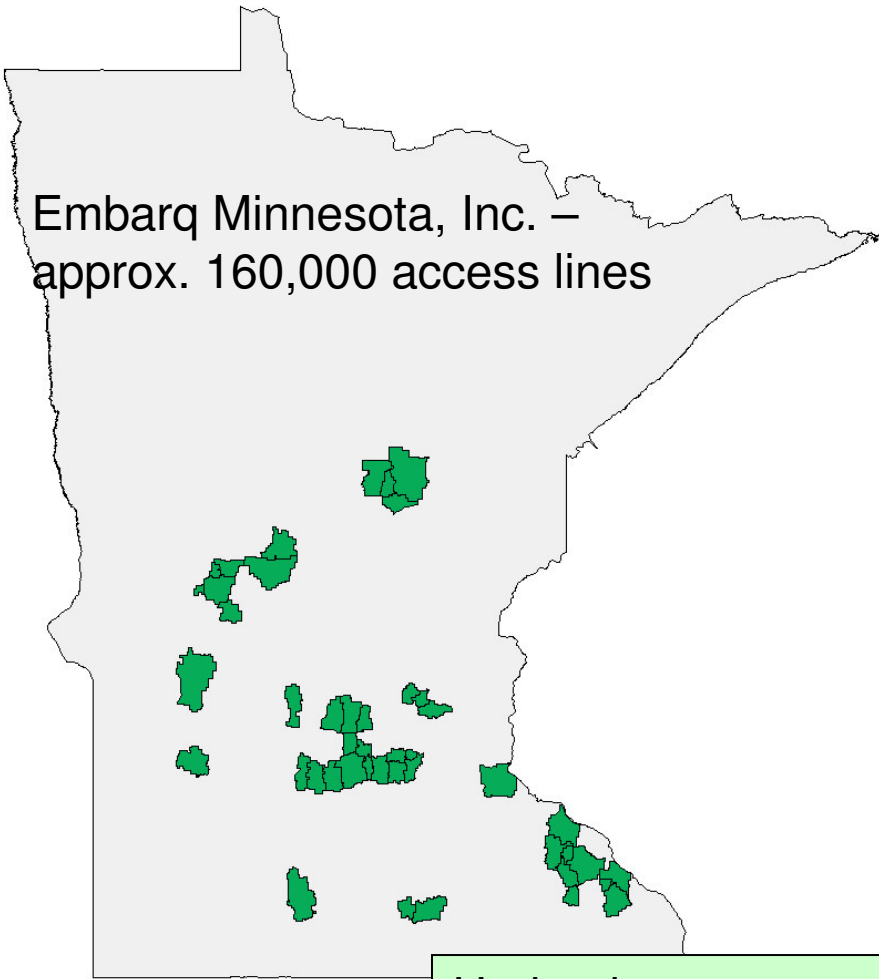


USF Reform Proposal

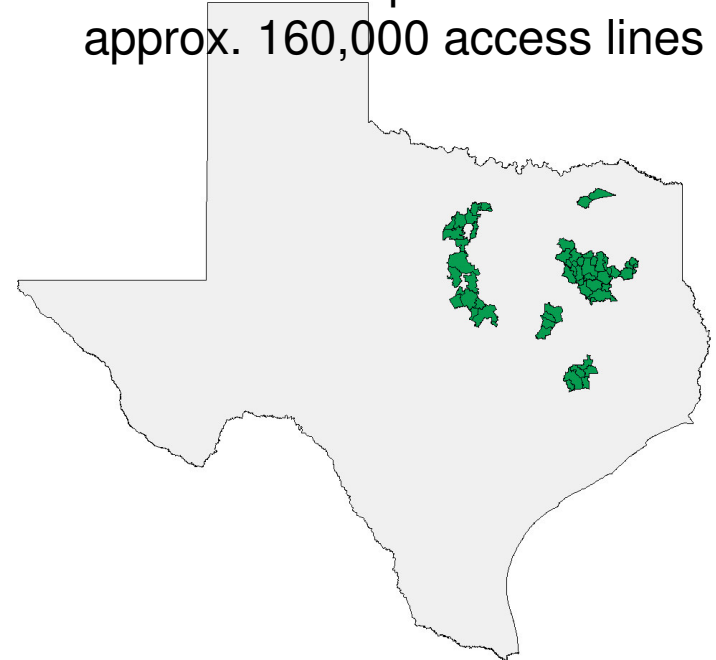
- Current USF system incorporates implicit subsidies
- Assumes revenues from low-cost areas can be used to offset costs of serving high-cost, rural areas
- They can't...
 - Competition prevents low-cost wire centers from subsidizing high-cost wire centers
 - Competition also prevents low-cost *portions* of a wire center from subsidizing high-cost portions of the same wire center
- Solution: Support must be calculated at a more granular level: sub-wire center



Embarq Minnesota, Inc. –
approx. 160,000 access lines



United Telephone of Texas
d/b/a/ Embarq –
approx. 160,000 access lines



Under the current system, Embarq's *entire* territory in a state is either considered “high cost” or “not high cost”.

In Minnesota, Embarq receives \$0 of High Cost Support because costs are averaged across the entire study area. In contrast, in Texas Embarq receives \$18M of High Cost Support annually.



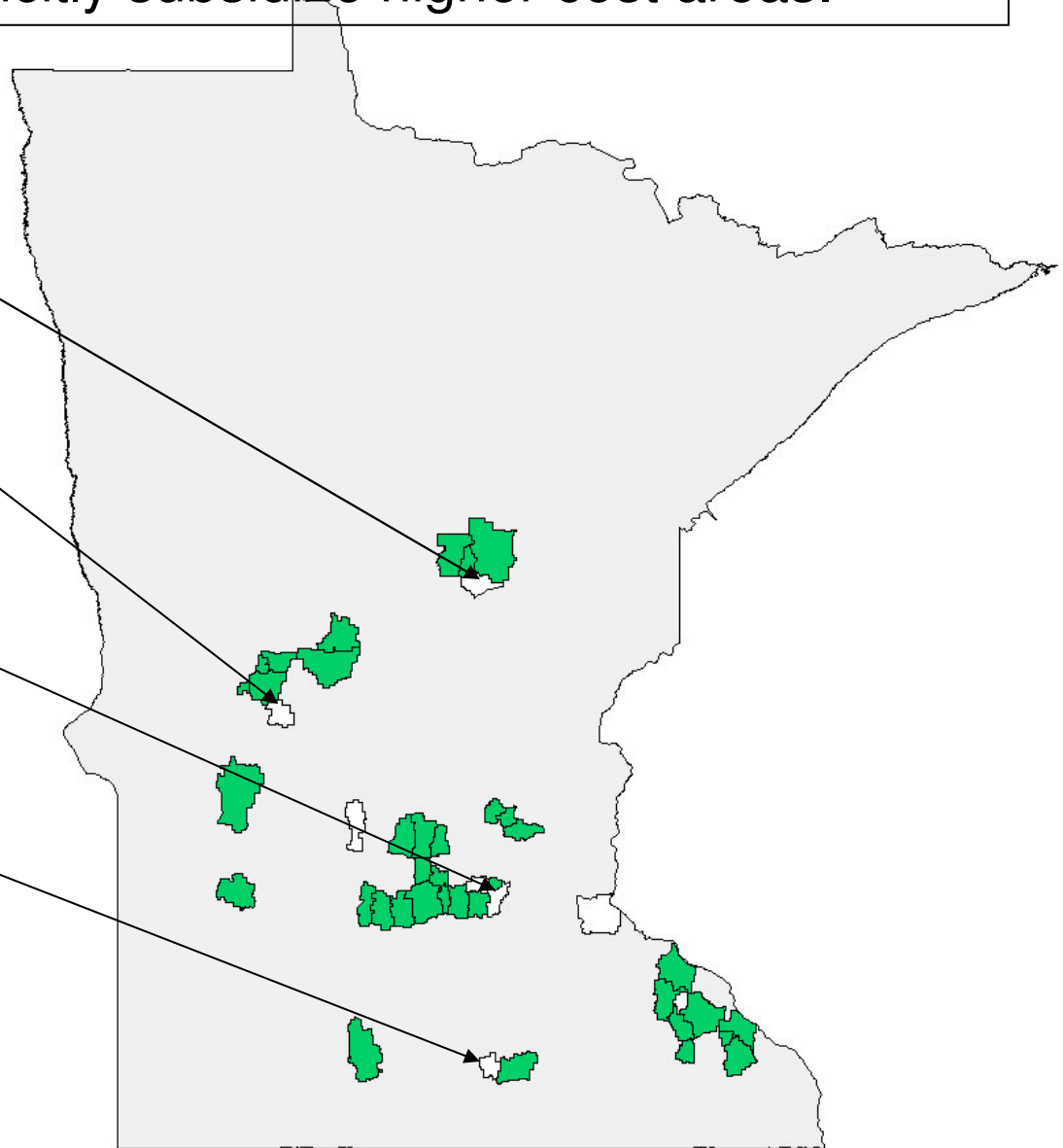
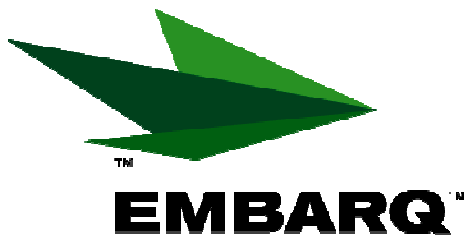
In reality, we serve many high-cost areas such as Villard and Bennettville. Pre-competition, it was possible for low-cost areas (Chaska) to implicitly subsidize higher cost areas.

Bennettville
\$ 114.70 per line per month

Villard
\$ 111.75 per line per month

Chaska
\$ 28.85 per line per month

Waldorf
\$ 137.86 per line per month

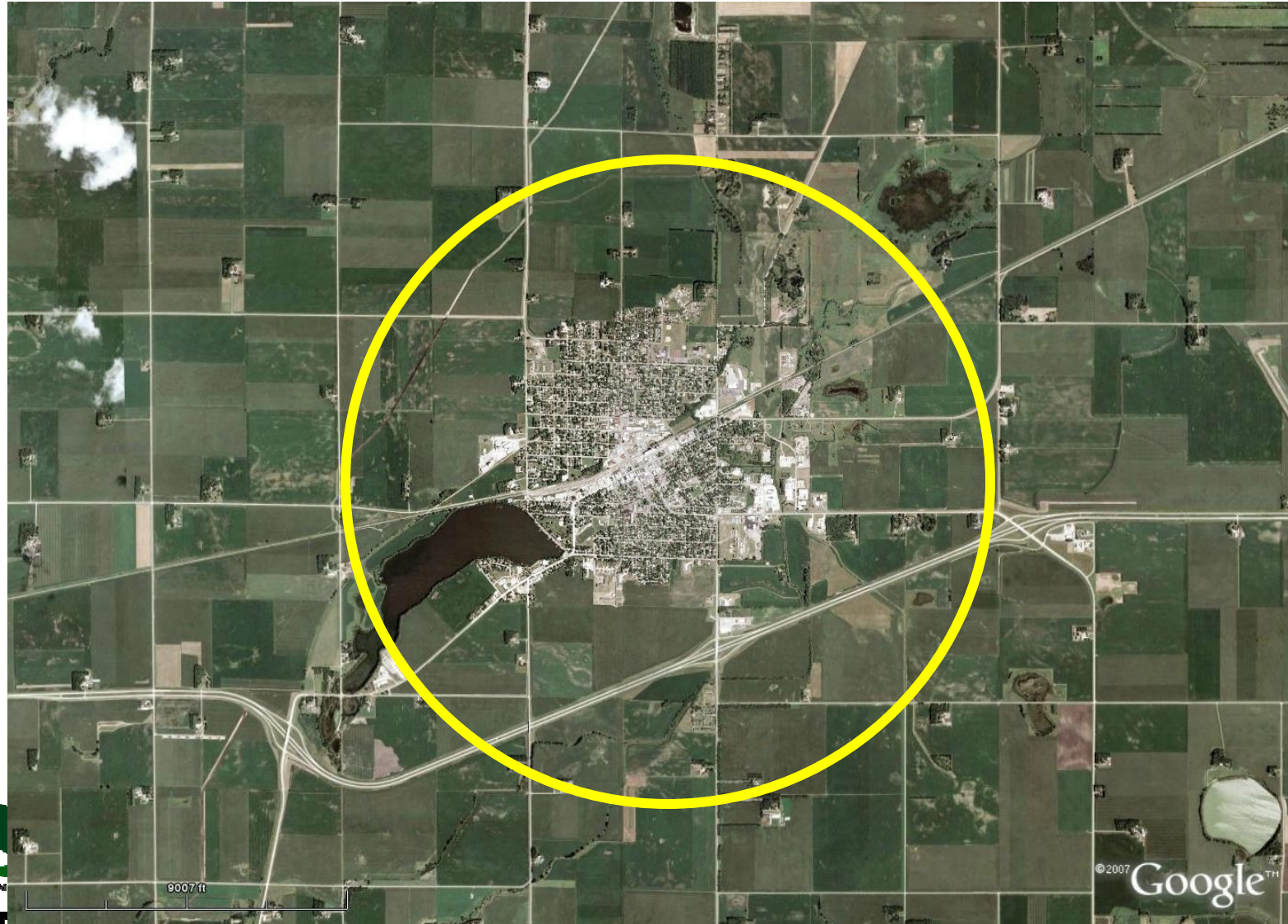


Under the current USF system...

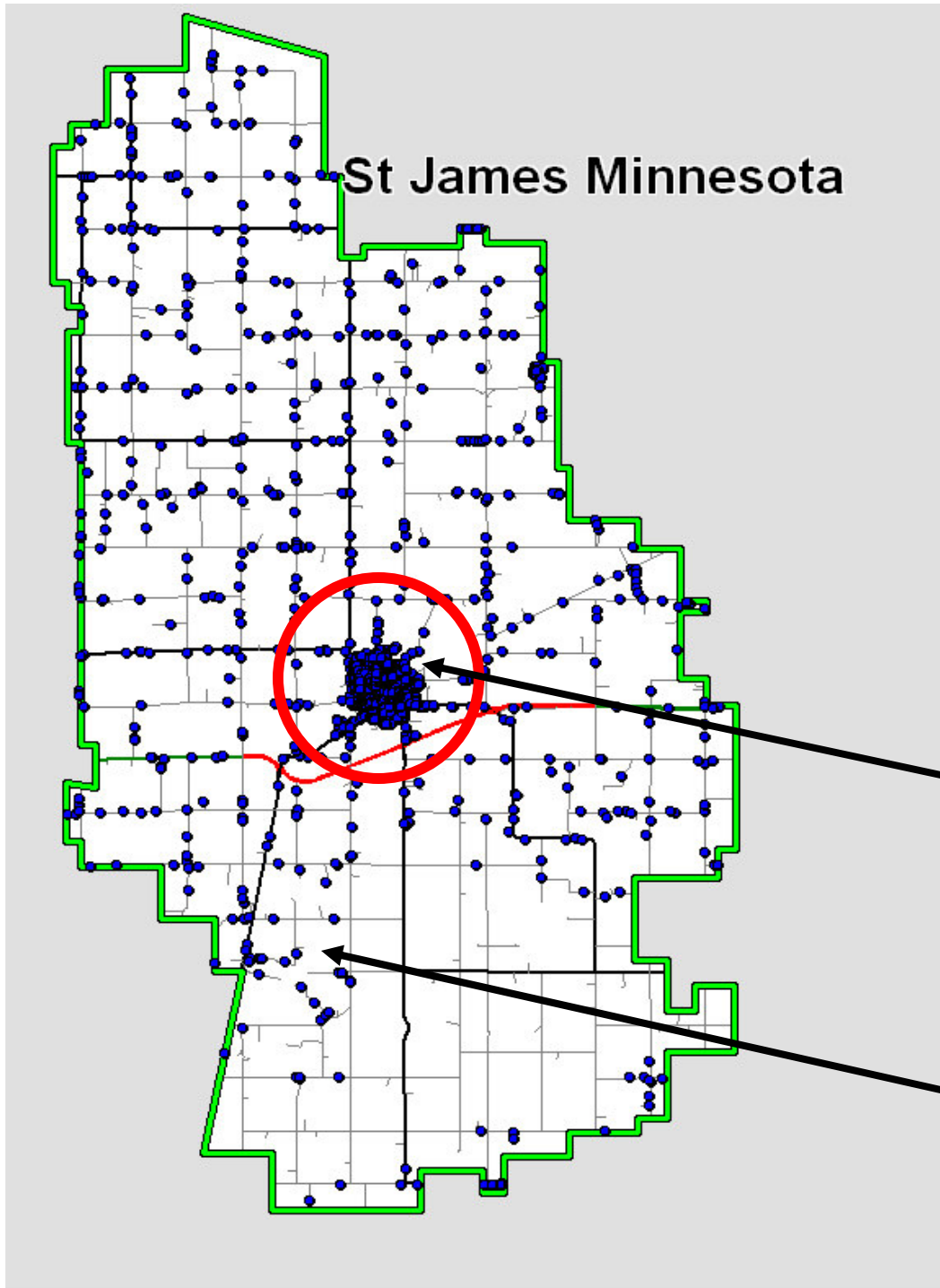
1. Implicit subsidization exists *between* wire centers, and...
2. Implicit subsidization also exists *within* a single wire center.
3. Neither form is sustainable in the face of competition.
4. So support must be calculated more granularly...sub-wire center.



St. James, Minnesota City Center



St James, Minnesota Investment Overview



St James Minnesota

Wire Center

Total Lines Served: **3,157**

Investment per Line:
\$2,025

City Center

Total Lines Served: **2,427**

Investment per Line:
\$1,016

Outside City

Total Lines Served: **730**

Investment per Line:
\$5,054